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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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| In the Matter of | ) | |
| | ) | |
| Implementation of the | ) | CC Docket No. 96-128 |
| Pay Telephone Reclassification | ) | |
| and Compensation Provisions of the | ) | |
| Telecommunications Act of 1996 | ) | |

**AT&T REPLY**

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# TABLE OF CONTENTS

## SUMMARY

In their comments, the PSPs have offered a host of indefensible theories to revive the Commission's unlawful 35 cent default compensation rate. In contrast, the non-PSP commenters, including representatives of both carriers and customers, convincingly show that the compensation rate should be significantly below that amount, because PSPs' costs for originating coinless calls are far less than their costs for providing end-to-end local coin service. Indeed, even after analyzing the cost figures in the record and making appropriate adjustments, AT&T shows below that a "bottom up" cost-based rate for payphone compensation is only slightly over 12 cents per call.

The comments show that the per-call compensation rate must be based on costs, because it is the only method that is consistent with all of the Commission's prior decisions. More important, however, it is the only way to assure that the compensation amount is fair to PSPs, carriers and consumers alike, as required by the Act. Indeed, as AT&T's expert economist shows, adoption of the PSPs' so-called "market based" methodology would guarantee them a monopoly price for payphone access.

The PSPs are also wrong that the D.C. Circuit endorsed a "market based" approach to per-call compensation. The Court made no such finding. Rather, it held that the

Commission acted arbitrarily in attempting to base its default rate on the deregulated price of a local coin call, because it included many costs that were plainly not incurred in originating coinless calls at payphones.

The PSPs' comments make clear that they are expressly seeking subsidies from the providers of coinless calls to support costs that are exclusively incurred in providing local coin calls. No such subsidies are justified. In particular, the fact that the Commission has now permitted PSPs to fully recover all of their costs for local coin calls, which represent over 70% of all payphone calls -- a fact that the PSPs conveniently ignore -- makes it clear that there is no need for the PSPs to recover a "market rate" for originating coinless calls. And in all events, a true blended "market rate" for such calls, based on the same methodology used by the RBOC/LEC Coalition, yields a compensation rate of 10.67 cents.

AT&T and others strongly urged the Commission against using an "avoided cost" methodology, because it is theoretically unsound (matching prices with costs) and could significantly overcompensate PSPs. If, however, the Commission decides to pursue this course, it should recognize that its prior orders significantly overstated the correct "market" price for local coin calls and use a 25 cent ceiling. Moreover, AT&T's analysis below, based on a review of the entire record, calculates that the actual avoided costs for coinless calls are between 12.5 and 17.5 cents per call. In addition, the PSPs' claims for added costs related to FLEX ANI delivery and "collection" costs are unjustified, and in all events the amounts they seek are excessive. Furthermore, the Commission has already properly rejected PSP attempts to base payphone compensation on 0+ commissions. There is no basis for modifying that decision.

There is general agreement that both smaller IXCs and LECs must be included in the interim per-phone compensation regime. As AT&T shows, however, the per phone payments should be based on carriers' total toll revenues, because they are the only generally available data for making such assessments. Finally, it is critical that the Commission clarify the confusion and rectify the inequities created by its earlier compensation rules. Thus, it is imperative that the Commission act promptly on this remand and that it order a full true-up of all money paid and received under its unlawful rules.

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| In the Matter of<br><br>Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 | ) ) ) ) ) ) | CC Docket No. 96-128 |

**AT&T REPLY**

AT&T Corp. ("AT&T") hereby replies to the comments on issues arising from the D.C. Circuit's determination that central aspects of the Commission's payphone compensation plan could not be sustained.[1]

## I. PER CALL COMPENSATION MUST BE COST-BASED.

As they did last year, all of the commenters, except for the PSPs, agree with AT&T (pp. 4-13) that the Commission should set a uniform per-call compensation rate that is cost-based.[2] This view is "fair" as required by

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1 A list of the commenters and the abbreviations used to refer to each is appended as Attachment 1.

2 See, e.g., Sprint, p. 3 ("Thus, the issue now before the Commission on remand is not whether payphone compensation should be based on costs. Rather, the issue is how to determine the appropriate measure of costs"); CompTel, p. 10-11; CWI, p. 10 (Commission should set a national cost-based rate); Frontier, p. 3-9; MCI, p. 1-5; Paging Network, Inc., p. 12-13 (Commission should establish a reasonable cost-based compensation amount if it does not rely on a "caller

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Section 276(b)(1)(A),[3] and it is consistent with the Commission's previous findings and the D.C. Circuit's decision.

In Illinois Public Telecommunications Ass'n v. FCC,[4] the D.C. Circuit held that the Commission acted unlawfully in establishing a so-called "market" compensation rate for coinless calls, because it ignored substantial record evidence that the costs of originating coinless calls are significantly less than the price for end-to-end local coin calling on which the payphone compensation rate was based.[5] The Court also stated that it was not enough to justify linking an excessive compensation rate to the deregulated local coin rate just because the compensation

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pays" mechanism). See also, letter from Reginald R. Bernard, SDN Users Association to William F. Caton, CC Docket No. 96-128, dated August 22, 1997.

3 CompTel, p. 2 ("fair compensation requires that compensation be based upon the costs incurred by compensable calls"); id., p. 11 ("cost-based compensation is the only compensation rate that is 'fair' to all entities (including consumers)"). Moreover, the Competition Policy Institute, a consumer-focused non-profit organization, also (p. 7) urges the Commission to "adopt a 'bottom up' approach to the correct level of compensation."

4 D.C. Circuit Nos. 96-1394 et al. (July 1, 1997) ("D.C. Circuit Order").

5 D.C. Circuit Order, Slip Op. at 16.

rate might be adjusted thereafter through negotiation. It emphasized that IXCs may have to rely on the default rate in the absence of successful negotiations or call blocking, and they are therefore "entitled" to a reasonable rate.[6]

As AT&T showed in its comments (pp. 5-6), the Commission has consistently held that costs are the proper basis for setting payphone compensation rates, although the Commission had earlier expressed the concern that it lacked reliable data necessary to set a cost-based compensation rate.[7] In its Notice of Proposed Rulemaking here, the Commission again tentatively concluded that "PSPs should be compensated for their costs in originating the types of calls for which we have concluded that compensation is appropriate," and it again sought reliable cost data.[8] Even the rate the Commission ultimately established was purportedly based on costs, because the Commission assumed (albeit incorrectly) that the deregulated price for

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6 Id. at 17.

7 Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, 7 FCC Rcd 3251, 3255-56 (1992).

8 Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, 11 FCC Rcd 6716, 6736 (1996).

providing end-to-end local coin calls was an appropriate surrogate for the cost of originating coinless calls.[9]

AT&T provided cost data to the Commission in response to the Notice and updated those data in this remand proceeding. Certain other PSPs have also submitted data on payphone costs. As described in AT&T's prior comments, the text below and in the accompanying reply affidavit of David Robinson,[10] the cost data in the record were and are ample to permit the Commission to set a fair and accurate cost-base compensation rate, and they show that the "surrogate" used initially by the Commission is, as the D.C. Circuit held, inappropriate.

In contrast, many PSPs insist that they are entitled to "market-based" compensation that is totally unrelated to, and far in excess of, their costs for originating coinless calls.[11] Significantly, the largest

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9 See, e.g., Competition Policy Institute, p. 2. This disposes of Peoples' erroneous claim (p. 2) that the Commission rejected a cost standard for payphone compensation.

10 Attachment 2 hereto,

11 E.g., RBOC/LEC Coalition, pp. 13-14, 20-30; APCC, pp. 3-4. See also, CCI, p. 5-6, Peoples, pp. 4-5. Peoples also argues that the D.C. Circuit remanded the Commission's payphone orders "for further justification," so that the Commission can justify the use of a 35 cent rate by simply explaining in more detail why it chose this approach to compensation. Id. at 4, n.3, citing Competitive Enterprise Institute v.

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group of PSP commenters, the RBOC/LEC Coalition, has ignored the Commission's request for specific, disaggregated information on their costs of handling payphone calls.[12] Instead (p. 11-14), the Coalition incorrectly proclaims that the D.C. Circuit affirmed the use of a market-based compensation rate and that the use of a cost-based rate would be inconsistent with Section 276.

Contrary to the RBOC/LEC Coalition's assertion (p. 12), the D.C. Circuit's decision neither requires nor

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National Highway Traffic Safety Administration, 45 F.3d 481, 484 (D.C. Cir. 1995). This argument ignores, however, the critical fact that the D.C. Circuit found that the Commission's entire approach to setting the compensation rate was arbitrary and capricious, while it did not make such a finding when it remanded the agency's action in Competitive Enterprise. See Competitive Enterprise Institute and Consumer Alert v. National Highway Traffic Safety Administration, 956 F.2d 321 (D.C. Cir. 1992). The D.C. Circuit's finding of arbitrariness and capriciousness effectively vacated the Commission's actions. See ex parte letter in CC Docket No. 96-128 dated August 15, 1997 from Peter Jacoby, AT&T to Richard Metzger, Deputy Chief, Common Carrier Bureau. See also, CompTel, pp. 4-7.

[12] Public Notice, DA 97-1673 (August 5, 1997), p. 2. For example, the RBOC/LEC Coalition's average total costs per call in its recent filing have increased from 34 to 37 cents per call (Andersen Report, n.14), even though it reported last year that the average per-call costs were only 25-32 cents (RBOC Coalition Comments, July 1, 1996, p. 15, n.15). However, the RBOC/LEC Coalition does not offer a shred of evidence to support this alleged increase. This is particularly suspect in light of Peoples' acknowledgment (n.12) that its per-call costs have declined over the same period.

endorses a market-based approach to per-call compensation. The Court found only that Section 276 grants the Commission express authority to establish a local coin rate and that the Commission may do so using a market-based approach. The Court did not make any findings regarding the merits of such an approach as it applies to the per-call compensation rate, except to find that the Commission acted arbitrarily and capriciously in setting the compensation rate equal to an assumed deregulated local coin rate -- in significant part because the costs of providing coin calling include amounts plainly not incurred in originating coinless calls. Thus, far from affirming the Commission's use of a market-based approach for payphone compensation, the Court found that approach to be substantively unfair and illogical.[13] Moreover, as shown in the attached declaration of AT&T's expert economist Dr. Frederick R. Warren-Boulton, the only way that payphone compensation prices can be properly established "is through a cost-based procedure."[14]

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13 CWI, p. 6. See also Competition Policy Institute, p. 8 ("[t]he Commission does not serve the public interest by permitting firms with market power to collect rates bearing no relationship to costs of providing a service in the name of promoting competition").

14 Attachment 3 hereto, pp. 2-4. Moreover, contrary to the theory proposed by the RBOC/LEC Coalition (pp. 21-24), Dr. Warren-Boulton's declaration (p. 2) also shows that "Ramsey pricing" is only applied in economic terms when a single firm (here the PSP) has market power over

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## II. PSPS SHOULD NOT RECOVER THE COSTS OF LOCAL COIN CALLS AS "COMPENSATION" FOR ORIGINATING COINLESS CALLS.

The PSPs' demands for a "market-based" payphone compensation rate ignore the effects of a critical change that has occurred as a result of the Commission's payphone orders. For the first time, all PSPs are now assured they can receive a fully compensatory "market" rate for all local coin calls, free of any state regulatory limitations or the need for subsidies.[15] This was a constant PSP complaint in last year's comments,[16] and it resulted in the Commission's decision to deregulate the local coin rate, a decision the D.C. Circuit affirmed. PSPs should now be required to use that authority to dissociate completely the costs of coin calls from the costs of coinless calls. This is best

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two or more products. Given the Commission's assumption, and the PSPs' continued assertion, that the market for local coin calling is competitive, Ramsey pricing cannot be applied to the compensation rate for coinless payphone calls (id., p. 3). Indeed, Dr. Warren-Boulton shows (id.) that the RBOC/LEC Coalition's theory would result in the application of a "profit maximizing monopoly price" to compensable coinless calls -- not a competitive market price.

15 In contrast, carriers have clearly recognized this change. See, e.g., CompTel, p. 12.

16 See, e.g., APCC Comments, July 1, 1997, pp. 14-16; Peoples Comments, July 1, 1996, pp. 15-16; CCI Comments, July 1, 1996, pp. 8-9.

accomplished by establishing a separate cost-based compensation rate for coinless payphone calls.[17]

A subsidy-free, cost-based rate for coinless calls is consistent with the APCC's views of last year:

> "Imposing a high per call charge on interstate and/or intrastate coinless calls and allowing these calls to continue to bear the expense of a local coin calling rate that is not bearing its share of costs perpetuates the disparity between the cost causer and the source of the cost recovery."[18]

A subsidy-free cost-based rate for coinless calls is also consistent with the undisputed facts. Local coin calls represent over 70% of the calls made at payphones.[19] PSPs generally assert -- and AT&T agrees -- that the economics of the payphone business are driven by the

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[17] Indeed, Dr. Warren-Boulton (p. 6) demonstrates that linking the payphone compensation rate to the deregulated local coin rate is affirmatively harmful to consumers, because it creates incentives for PSPs to price local coin calls above even the profit maximizing level for such calls. See also Sprint, p. 5 (setting the rate at a cost-based level prevents the possibility that PSPs will seek to benefit from the placing of subscriber 800 calls intended solely for the purpose of increasing their per-call compensation).

[18] APCC July 1, 1996 Comments, p. 16. See also CWI, p.7 ("compensation for a particular call must bear a relationship to its costs, not the costs of some other calls placed from the payphone" (emphasis in original)).

[19] E.g., Peoples, p. 6.

economics of coin calls.[20] However, instead of treating coinless payphone calls as the "by-product of payphone installation"[21] which they are, and using their newly-granted right to recover all of the costs of coin calls in their coin rates, the PSPs prefer to look to carriers of coinless calls (and their customers) to provide ongoing subsidies for payphones. This is in fact the PSPs' explicit goal:

> "Here [if permitted] the industry would tend to load cost recovery onto dial-around and subscriber 800 calling, increasing the price of those calls relative to local coin rates."[22]

The Commission should reject the PSPs' efforts to create more subsidies for local coin calls. PSPs are now

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[20] See, e.g., Peoples, p. 6 ("PSP payphones can rarely, if ever, be justified based on the revenues from coinless calls alone. . . . Peoples will not install payphones in locations that do not generate substantial numbers of coin calls"). See also RBOC/LEC Comments, p. 16 ("most payphones could not be supported if they were not capable of handling coin calls"); Sprint, p, 3 (quoting trade press article in which the CEO of a PSP states that revenue from coinless calls is "gravy"); CWI, p. 7; CompTel, p. 12; LCI, p. 6. Moreover, coin phones inherently enable callers to make coinless calls. Thus, coinless calls add no incremental costs to the operation of a coin phone, making Peoples' assertion (p. 7) that location agents require payphones to handle all types of calls irrelevant. Further, because coinless calls generate no per-minute usage costs, the duration of such calls is also irrelevant (see id.).

[21] CompTel, p. 12.

[22] RBOC/LEC Coalition, p, 22. See also APCC, p. 12.

assured that the costs of local coin calls (i.e., the vast majority of their calls) can be recovered in their rates, an assurance they never had before. Thus, it is clear that a cost-based compensation rate for the remaining calls, as proposed by AT&T and many others,[23] will be more than sufficient to assure the "widespread deployment of payphones."

Indeed, the PSPs seek to elevate this introductory phrase in the statute beyond all reasonable proportions. On the basis of no data or analysis, they assume that the installation of every new payphone increases consumer welfare and the removal of every payphone harms consumers. This conclusion is absurd. In particular, it ignores the statute's basic fairness requirement[24] and its express recognition in Section 276(b)(2) that there may be a need for "public interest" payphones.

For example, APCC (n.4) asserts that "[t]here should be a bias toward setting the compensation rate at the high end of the zone [of reasonableness because t]he worst

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23 See n.2 above.

24 See Frontier, pp. 3-4 (fair compensation "requires a balancing of consumer and investor interests"); see also id., n.16 (citing the legislative history of TOCSIA, which provided that the safeguards of the Act "were intended 'to assure fairness for consumers and service providers alike'").

consequence of setting a rate too high is that there will be an oversupply of payphones until corrective measures take effect."[25] In fact, the worst consequence of an excessive payphone compensation rate is that carriers and consumers will be paying hundreds of millions of dollars unnecessarily to PSPs, or that calls from payphones will be blocked by carriers or 800 subscribers who refuse to pay PSPs' unreasonable charges.[26]

Similarly, the RBOC/LEC Coalition's unsubstantiated threats that many payphones would have to be removed even at a 35 cent compensation rate is an attempt to

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25 The RBOC/LEC Coalition also assumes without analysis that the removal of any payphone "lead[s] to significant consumer harm" (Hausman Declaration, ¶ 45). The Coalition fails to address, however, the possibility that any of the current 2.3 million payphones may simply be uneconomic; that a shortfall at a specific payphone might be made up by a location owner who wishes to pay to have a payphone on its premises (similar to the situation at the hundreds of thousands of semi-public phones); or that any potential harm could be addressed through the installation of public interest telephones, as specifically contemplated by Section 276(b)(2).

26 The D.C. Circuit recognized that it would be unwise to create a situation in which (i) carriers must expend significant resources (that would have to be paid for by consumers) to develop the capability to block overpriced access to payphones, and (ii) there could be significant numbers of blocked calls. D.C. Circuit Slip Op. at 17; MCI, p. 4. Moreover, the apparent recent increases in payphone calling counsels a lower, rather than higher, per-call rate (see Peoples, n.12 (noting a significant decline in its total per-call costs since last year due to increased volumes)).

bully the Commission into overcompensating PSPs. The Coalition makes this claim through a third party consultant who provides absolutely no data to support it.[27] More fundamentally, however, the Coalition fails to explain why the addition of compensation for 800 subscriber calls, a totally new revenue stream, combined with the revenues from local coin calls (which can now be priced to fully recover their costs), would not in fact increase the profitability (and number) of payphones generally.

In all events, to the extent the Commission is seeking a "value of service" or "market" rate for coinless calls from payphones, the closest true analog is the rate negotiated by AT&T and APCC in 1994 for dial-around access code calls.[28] At that time, AT&T sought a waiver to be permitted to pay dial-around compensation on a per-call

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27 The entire support for the Coalition's claim is found in footnote 15 of the Andersen Report, which states "[u]sing station-by-station data provided by several Coalition members along with the marginal revenue thresholds used by Coalition members to evaluate whether a station should be kept in service, we estimate that . . ." Andersen provides none of the underlying data for its "estimate," which is in turn relied upon to support a conclusion by Hausman (¶ 45) that is boldly cited as fact in numerous places in the RBOC/LEC Coalition's brief (pp. vi, 14, 28, 31).

28 Contrary to APCC's current claim (pp. 7-9) the dial-around rate it agreed to is a much closer "market surrogate" for such calls than commissions on 0+ calls. See also RBOC/LEC Coalition, p. 12 (dial-around and 0+ calls are "similar services").

basis at a rate of 25 cents per call.[29] APCC supported AT&T's waiver request, and the waiver was granted on December 29, 1994.[30]

At the time of the waiver, AT&T's average price for dialaround calls was about $2.50, and the agreed upon compensation represented a payment of about 10% of the price of the call. Since that time, the average price of an AT&T dial-around call has dropped to under $2.20, so the appropriate current rate for such calls would be 22 cents. Moreover, the record shows that the average price of an 800 subscriber call is at most $.50,[31] and that 800 subscriber calls outnumber dial-around calls by a ratio of about 2 to 1. Accordingly, using a blended rate approach such as that suggested by the RBOC/LEC Coalition (p. 26), the market rate for payphone compensation is 10.67 cents per call,[32] which

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29 In conjunction with the waiver, AT&T agreed to pay a rate of 25 cents on all dial-around calls it received, not just interstate calls. The compensation rate the Commission must adopt here would similarly apply to all dial-around calls.

30 See Policies and Rules Concerning Operator Service and Pay Telephone Compensation, 10 FCC Rcd 1590, 1591 (Com. Car. Bur. 1994).

31 See RBOC/LEC Coalition, Andersen Report, p. 9, citing AT&T Reply Comments, July 15, 1996, p. 11.

32 [1 * $.22 + 2 * $.05] / 3 = $.1067.

is directly in line with the cost-based rate AT&T has calculated for coinless calls.

## III. THE COST-BASED METHODOLOGY PROPOSED BY AT&T WILL FULLY COMPENSATE PSPS FOR THE SERVICES THEY PROVIDE IN ORIGINATING COINLESS CALLS.

In its comments (pp. 5-6, 10-16), AT&T showed that a fair compensation rate based on the costs of coinless calls -- which the Commission has repeatedly recognized as the proper basis for calculating compensation -- would result in a far lower rate than the 35 cents the Commission set in the Report and Order. AT&T's analysis showed that the costs to a PSP of handling a coinless call are slightly less than 11 cents per call.[33] After reviewing the cost figures presented by various PSPs, it appears that AT&T's view of the costs for coin calls was supported by the cost figures of the PSPs.[34] However, AT&T agrees that some adjustments are appropriate in the areas of overhead, general and administrative expenses and taxes, increasing the total per-call cost for coinless calls to 12.2 cents.[35] This amount is fully consistent with the 16.7 cents that

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33 Unlike all other cost analyses, AT&T's data were supported by a sworn affidavit.

34 Robinson Reply Aff., ¶¶ 2-5 (costs for coin collection and maintenance for coin phones are similar).

35 Id., ¶¶ 7-9.

NYNEX presented in Massachusetts as its total costs to handle an end-to-end local coin call.[36]

The PSPs' criticisms of AT&T's methodology (which is similar to the methodology AT&T used last year) are not valid. First, AT&T's analysis is based on TELRIC, which is the appropriate methodology in these circumstances.[37] Moreover, contrary to APCC's claim (p. 11) it is indeed possible to disaggregate the costs of coinless calls from the costs of local coin calls, a fact that is clearly demonstrated by the careful delineations made in Mr. Robinson's affidavits. For example, there are portions of payphone equipment that are unnecessary for (and not used in) placing coinless calls from payphones, and the coin aspects of payphones are more expensive to maintain and repair than the coinless ones.[38] Accordingly, it is reasonable to assign more maintenance and related costs to coin calls than to coinless calls. By contrast, Mr. Robinson's analyses assign the costs of the coinless aspects of payphones equally to all calls from payphones, including

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36 AT&T's analysis may be generous, because the record shows that the costs of completing a local coin call in Massachusetts are 5 cents a call (see APCC, Attachment 2), leaving a net of 11.7 cents in total costs, even before subtracting specific coin-related costs.

37 Warren-Boulton Declaration, pp. 6-7.

38 See Robinson Aff., ¶ 11-14; Robinson Reply Aff., ¶ 6.

the costs of the basic payphone line and necessary blocking and screening features.[39]

Further, APCC's argument (n.11) that the cost of a coinless payphone should be applied only against coinless calls and the RBOC/LEC Coalition's argument (p. 17) that AT&T's analysis assumes only the presence of a coinless phone miss the point. The coinless call costs AT&T showed were not premised on the assumption that PSPs should be placing coinless, rather than coin, payphones. Rather, AT&T's cost figures show the difference in the costs of coin and coinless calls to the PSP, based upon a reasonable mix of equipment PSPs use in providing coin services. Thus, despite the PSPs' claims, AT&T's cost methodology is appropriate for establishing the default payphone compensation rate.

Some PSPs also claim that the Commission should not use a cost-based methodology, because it would require the Commission to engage in lengthy and complex regulatory cost proceedings.[40] PSPs also claim that their costs are

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[39] Robinson Aff., ¶ 17. Moreover, consistent with CCI's argument (p. 16), AT&T's analysis of equipment costs is based directly on the cost of "installing and operating an additional payphone." And contrary to CCI's claims (p. 14) AT&T's costs for payphones recognize that a substantial proportion of phones are placed outdoors (see Robinson Aff., ¶ 6)

[40] E.g., RBOC/LEC Coalition, p. 27.

significantly higher than those shown by AT&T, because they should include other items. Both claims are wrong.

First, the Commission need not conduct lengthy or frequent cost proceedings for payphone compensation. Most of the costs of payphone operations are consistent regardless of where payphones are geographically located, and the PSPs failed to point to major geographic cost differences. Moreover, the Commission need not -- and should not -- set a rate based on the costs of each individual PSP. Rather, its default compensation rate should be based on the costs of an efficient payphone provider.[41] Otherwise, the Commission would be rewarding inefficiency at the expense of carriers and consumers. This is not fair, as required by Section 276, and it clearly does not serve the pubic interest. Indeed, it is critical that the Commission not charge carriers and consumers for speculative, wasteful or inefficient PSP costs.

There are a number of examples of such costs in the record. For example, despite AT&T's showing that the total costs of purchasing and installing a new coin phone range from $2,215 (for dumb payphones) to $2,799 (for smart

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[41] See Sprint, pp. 6-7 (providing ample Commission precedent for such a procedure); AT&T, pp. 8-9; CWI, p. 14. See also Frontier, n.4.

sets),[42] many independent payphone providers ("IPPs")[43] have presented payphone "costs" that are much higher.[44] This is due to the fact that IPPs often engage in speculative buying of "locations." As shown in Attachment 4, on a per-phone basis, such locations have been offered at prices up to \$5,500.[45] PSP shareholders are free to speculate as they wish, but they should not be allowed to pass the risks of their speculative investments to carriers and consumers through the payphone compensation process.

IPPs also seek recovery of commissions on payphone calls, including commissions on dialaround and subscriber

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[42] See Robinson Aff., ¶ 9 (providing basic purchase and installation prices only). The prices listed here include an 11.25% cost of capital.

[43] As noted above, the RBOC/LEC Coalition provided no detail on their underlying costs of operating payphones.

[44] IPPs' equipment costs are reflected in several different ways in their comments. Sometimes they are identified as equipment costs, but other times they are referenced as depreciation, amortization or interest (see Robinson Reply Aff., ¶ 13).

[45] This rebuts CCI's claim (p. 14) that IPPs are "required to be efficient." Indeed, at its \$64.33 cost per month per station cost for "Depreciation /Interest" (see Peoples, p. 10), Peoples' principal and interest cost per phone on a 10 year depreciation basis is over \$7700.

800 calls.[46] As AT&T showed in its comments (p. 15), these costs should be excluded from the calculation of payphone compensation.[47] Moreover, the Commission has previously explained that if PSPs were guaranteed recovery of their commission costs through a regulatory mechanism, there would be immediate and perverse incentives to include higher and higher commissions within the compensation system, which would, in turn, cause spiraling prices for consumers.[48] There is no reason to increase the spiral of payments to location owners.[49] Moreover, as AT&T (p. 15) showed, if the

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[46] E.g., APCC, Attachment 3, p. 3; CCI, pp. 9, 12-13; Peoples, p. 10. See also Andersen Report, p. 3 (including commissions as an expense).

[47] See also CWI, p. 9; CompTel, p. 14.

[48] Billed Party Preference for InterLATA 0+ Calls, Second Further Notice of Proposed Rulemaking, 11 FCC Rcd 7274, 7278 (1996). See also Warren-Boulton Declaration, p. 7 (any mechanism that includes commissions as part of the recoverable costs for payphone compensation validates the market power of location owners and promotes flow-through of monopoly profits to such entities).

[49] Peoples (p. 10) assigns 9 cents per call to commission costs. See also Sprint, p. 5; CCI, pp. 12-13 (noting that some PSPs are already promising to share payphone compensation with location owners). Indeed, the battle over commissions has increased to such a level that it makes carrier participation unprofitable in some market segments. For example, commissions at some inmate locations have now reached the 60% level. Adding money for commissions into the calculation of payphone compensation will only fuel higher payments. As Sprint (p. 10) states, there is no indication that Congress intended Section 276 should provide an additional boon to PSPs or location owners.

Commission decides that per-call compensation may include any commissions (under either a cost-based or avoided cost analysis), it must become embroiled in specifying a reasonable amount for such costs.

Finally, the comments demonstrate that the default rate the Commission adopts here should also be uniform,[50] because of the additional costs a floating rate would impose on carriers required to track compensable calls;[51] the fact that a floating rate would increase incentives for PSPs to engage in strategic pricing in order to maximize hidden compensation surcharges;[52] and the fact that a floating rate would be virtually impossible to administer.[53] AT&T also concurs with WorldCom (p. 5) that the rate established by the Commission should be used as the permanent default rate,[54] pending any subsequent proceedings the Commission

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[50] APCC (p. 10) also suggests that the Commission could adopt a "uniform" dial-around compensation rate (albeit at an excessive level).

[51] AT&T, pp. 16-18; Sprint, p. 6.

[52] LCI, p. 8; CWI, p. 10.

[53] AT&T, pp. 16-17; MCI, p. 5; Frontier, n.23.

[54] See also D.C. Circuit Order, Slip Op. at 18 ("[t]he agency may of course elect to use the new interim rate as a 'default rate' at the conclusion of the interim period"); APCC, p. 17 (suggesting that the Commission set a "permanent" compensation rate).